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COMMONWEALTH OF VIRGINIA

STATE CORPORATION COMMISSION

AT RICHMOND, MARCH 12, 2001

APPLICATION OF

VIRGINIA ELECTRIC AND
POWER COMPANY

CASE NO. PUE000343

For Approval of Generation Facilities
pursuant to Virginia Code § 56-580 D or,
in the Alternative, for Approval of
Expenditures pursuant to Virginia Code
§ 56-243.3 and for a Certificate of
Public Convenience and Necessity
pursuant to Virginia Code § 56-265.2

and

APPLICATION OF

VIRGINIA ELECTRIC AND
POWER COMPANY

CASE NO. PUF000021

For authority under Chapters 3, 4,
and 5 of Title 56 of the Code of
Virginia to participate in lease
financing arrangements for
construction of generation facilities,
and for a declaration of non-jurisdiction

FINAL ORDER

On June 16, 2000, Virginia Electric and Power Company
("Virginia Power" or "the Company") filed an application with
the State Corporation Commission ("Commission") in which it
proposed to reconfigure its various generating units at the
Possum Point Power Station and to construct a new combined cycle
generating unit (hereafter collectively referred to as "the

Project") at Possum Point. Presently, Virginia Power operates five units at Possum Point. Units 1 and 2 burn fuel oil and have a combined rated capacity of 143 MW. Units 3 and 4 burn coal and have a combined rated capacity of 322 MW, and Unit 5 is a 786 MW rated unit that will continue to operate on heavy oil. The Company proposes to take Units 1 and 2 out of service by no later than May 1, 2003, and to convert Units 3 and 4 to burn natural gas at a cost of approximately \$14 million. Virginia Power also proposes to construct a 540 MW combined cycle facility (Unit 6) that will operate at the Possum Point Power Station and will have an estimated cost of \$280 - \$300 million. This new unit is scheduled to be operational in May 2003, so as to coincide with the cessation of the burning of coal at Units 3 and 4. June 16, 2000 Application at 1-2.

The Company requires the Commission's authorization to construct and operate Unit 6. As a result of the construction of this unit and the retirement of Units 1 and 2, the total capacity at the Possum Point generating station will increase from 1251 MW to 1648 MW.

Virginia Power proposed in its application to employ synthetic lease financing for the new unit and to sublease a portion of the real estate at the Possum Point plant upon which the new generating facility will be built. It asked that:

(i) the Commission approve the project under § 56-580 D of the

Code of Virginia, (ii) declare that § 56-234.3 of the Code of Virginia does not require the Company to obtain prior regulatory approval before entering into the agreements necessary for the proposed synthetic lease financing, or (iii) in the alternative, grant an exemption from § 56-234.3 of the Code of Virginia or approve the Company's financial expenditures for the proposed lease and sublease transactions. The Company also sought the issuance of a certificate of public convenience and necessity under § 56-265.2 of the Code of Virginia in the event the Commission determined that § 56-265.2 applied.

Further, Virginia Power filed a "Motion for Determination of Applicability of, or in the Alternative, for Exemption or Waiver from, Bidding Rules" ("Motion") with the captioned application. In its Motion, the Company requested that the Commission find that the Rules Governing the Use of Bidding Programs to Purchase Electricity from Other Power Suppliers ("Bidding Rules"), 20 VAC 5-301-10 et seq., adopted in Case No. PUE900029, to be inapplicable to the Project.

On July 5, 2000, the Company filed a related application seeking authority from the Commission to participate in lease financing arrangements of approximately \$300 million for the construction of the new generating facility and for a declaration that the Commission would not assert jurisdiction over other parties participating in the transaction who,

according to the Company, would serve only as vehicles for the Project's financing. The July 5 application also sought approval under (i) the Virginia Utility Securities Act, Chapter 3 of Title 56 of the Code of Virginia, because the financing arrangements could be considered to create an evidence of indebtedness; (ii) Chapter 4 of Title 56 of the Code of Virginia, because the transaction will involve jurisdictional contracts or arrangements between Virginia Power and DEI-Sub, which is a subsidiary of Dominion Energy, Inc. and an affiliate of Virginia Power; and (iii) Chapter 5 of Title 56 of the Code of Virginia, because Virginia Power proposed to transfer real property at Possum Point by means of a ground lease, on which the new facility will be constructed. The Company will be reacquiring the constructed facility and related real property through a sublease.

On July 26, 2000, the Commission entered an Order Inviting Comments and Responses and Prescribing Notice. In this Order, among other things, the Commission sought comments by interested parties on the following issues:

- (1) Whether the Bidding Rules are applicable to the Project, or in the alternative, if they do apply, whether the Commission should grant Virginia Power an exemption to these Rules.
- (2) Whether the Commission should approve this Project exclusively under § 56-580 D of

the Code of Virginia, or under §§ 56-234.3, and/or 56-265.2 as well.

(3) If § 56-234.3 of the Code of Virginia applies to this Project, whether the Company should be granted an exemption from that provision, or approval under it to make "at risk" financial expenditures in association with the Project.

That Order docketed the proceeding, appointed a Hearing Examiner to consider the preliminary issues set forth in the Order and make recommendations thereon, and required Virginia Power to publish notice of its application for approval of the Project and its request for authority to participate in the related lease financing arrangements.

On August 21, 2000, the Staff and Company filed comments on the preliminary issues identified in the July 26, 2000, Order.

On September 1, 2000, the Chief Hearing Examiner issued her "Interim Report on Preliminary Issues" ("Interim Report") wherein she found the following:

1. The Bidding Rules are applicable, but a waiver of those rules should not be granted and does not appear necessary in this case;
2. The Company should be directed to supplement its pre-filed direct testimony with information on the alternatives bid in its January 1999 and December 1999 solicitations if relevant to this case. If not relevant, the Company should so advise the Commission in comments hereto;
3. If the recent solicitation is not relevant to consideration of market

alternatives herein, the Company should be directed to issue a Request for Proposals on a parallel track to consideration of this Project;

4. This application should be evaluated pursuant to Virginia Code §§ 56-46 (sic), 56-234.3, 56-265.2, and 56-580 D;

5. The Company should file an affidavit and schedule of expected expenditures as described . . . [within the Report] with its comments to this Report; and

6. Virginia Power should be granted interim authority to undertake permitting and preliminary site work, and to make financial expenditures for the proposed Project at its own expense and risk subject to the Commission's review of the supporting affidavit.¹

The Chief Hearing Examiner recommended that the Commission enter an order that adopts the Interim Report's findings; grants the Company approval pursuant to § 56-234.3 to proceed with financial expenditures, permitting and preliminary site work as was necessary to facilitate the timely completion of the Project, if finally approved by the Commission; and establishes a procedural schedule to receive evidence on the pending applications, applying the statutory standards for review set forth in §§ 56-46.1, -234.3, -265.2, and -580 D of the Code of Virginia.

¹ See September 1, 2000 Interim Report on Preliminary Issues, Case Nos. PUE000343 and PUF000021, Doc. Con. Ctr. No. 000910037 at 9.

On September 8, 2000, Virginia Power filed its comments on the September 1, 2000, Interim Report. Among other things, the Company contended that the Commission should not require a new solicitation for the Project, that Virginia Power's recent solicitations satisfy the Bidding Rules, and that § 56-580 D presented the sole legal standard under which the Project should be considered, given the General Assembly's decision to restructure Virginia's electric industry and establish standards for the approval of all new generation. The Company also withdrew its request for approval of "at risk" financial expenditures. It explained that a special purpose subsidiary of Dominion Energy, Inc., rather than Virginia Power, had made the necessary commitments with financial institutions for the Project. Virginia Power renewed its request that the Commission grant an exemption from the Bidding Rules or, in the alternative, conclude that Virginia Power had satisfied the bidding requirements through its recent solicitations.

On October 18, 2000, we entered our Order for Notice and Hearing. In that Order, we determined that the Bidding Rules applied to the Project, but that no further bids need be solicited by the Company. We directed that the responses to Virginia Power's recent RFPs be scrutinized to consider whether these responses presented better alternatives to provide electric service than did the Project. We further found that

the new generation project must be considered under §§ 56-46.1, -234.3 and -265.2 as well as -580 D, of the Code of Virginia, and that no ruling was necessary to determine whether the Company should be granted an exemption from § 56-234.3 since the Company had withdrawn its request for approval of "at risk" financial expenditures. Additionally, we set the matter for hearing, found that notice should be given and hearings on the applications held, and that the Staff should investigate the captioned applications and present its findings thereon in testimony. We remanded the applications to the Hearing Examiner to conduct further proceedings and to file a final report in this matter with the transcript.

On November 17, 2000, we entered an Order that authorized Virginia Power to enter into the lease financing arrangement, as described in its July 5, 2000, application, provided that its supporting documents were modified in accordance with the November 17, 2000, Order's requirements and were made subject to the conditions set out in that Order.²

A public hearing was convened on January 16, 2001. No Protestants or public witnesses appeared at the hearing. By agreement of counsel, all testimony and exhibits were admitted

² See Application of Virginia Electric and Power Company, For authority under Chapters 3, 4, and 5 of Title 56 of the Code of Virginia to participate in lease financing for construction of generation facilities, and for a declaration of non-jurisdiction, Case No. PUF000021, Doc. Con. Ctr. No. 001120402 (Nov. 17, 2000 Order).

into the record without cross-examination. Proof of notice of the applications was marked and admitted into the record as Exhibit 1.

On February 2, 2001, Deborah V. Ellenberg, Chief Hearing Examiner, issued her Report. In her Report, the Chief Hearing Examiner found as follows:

1. The proposed Possum Point Project as more particularly described in the June 16, 2000 application, is in the public interest and a certificate of public convenience should be issued subject to compliance with all recommendations set forth in the DEQ [Department of Environmental Quality] coordinated review, including the following conditions:

- (a) A review of the National Wetlands Inventory map should be performed, and a site delineation should be conducted in any suspect wetland areas prior to project construction to determine the absence or location, extent or type of wetlands present on the site. Upon receipt of such information, the DEQ will determine whether certain permits will be required for construction of the project;
- (b) As recommended by DEQ, the number of stream and wetland impacts should be avoided to the maximum extent practicable. For unavoidable impacts, the following practices should be utilized to minimize impacts to wetlands and waterways: operation of machinery and construction vehicles outside of the stream-beds and wetlands, use of directional drilling from

upland locations for the installation of utilities; the preservation and redistribution of the top 12 inches of trench material removed from a wetland for use as a wetland seed bank and root stock in the excavated area, and the use of synthetic mats when in-stream work is unavoidable;

- (c) All solid wastes generated at the site should be reduced at the source, re-used, or recycled. All hazardous wastes should be minimized;
- (d) In general, the use of herbicides or pesticides for landscape maintenance should be done in accordance with principles of integrated pest management. The least toxic pesticides that are effective in controlling the target species should be used;
- (e) As recommended by the Chesapeake Bay Local Assistance Department any Commission approval should be conditioned upon a requirement that Virginia Power comply with requirements of the Chesapeake Bay Preservation Act;
- (f) As recommended by the Department of Game and Inland Fisheries, Virginia Power should continue to coordinate with that agency in the future to determine additional nesting sites of the federally threatened bald eagle near the Possum Point Power Station;

2. If Virginia Power does not obtain or maintain control of the new facility, except as may be provided by the Commission in response to the Company's Functional Separation Plan, the certificate recommended

herein would sunset or expire, and further authority regarding the disposition of the new facility would have to be requested from the Commission; and

3. The Lessor under the synthetic lease financing for the Project and the Sublessor as described more fully above should be determined not to be public utilities subject to Commission jurisdiction based on and limited to the facts of this case.

The Chief Hearing Examiner recommended that the Commission enter an Order that adopts the findings in her Report; grants the Company's application for a certificate of public convenience and necessity for the Possum Point Project with the conditions set out in her Report; and dismisses the case from the Commission's docket of active proceedings. The Chief Hearing Examiner invited the parties to file comments to her Report within seven (7) days from the date of its issuance.³

On February 5, 2001, the Staff of the State Corporation Commission, by counsel, advised that the Staff did not intend to file comments on the February 2, 2001, Report of the Chief Hearing Examiner. Similarly, on February 7, 2001, the Company, by counsel, advised that it did not intend to file comments or exceptions in response to the February 2, 2001, Report.

As we noted in our October 18, 2000, Order for Notice and hearing, statutes other than § 56-580 D of the Code of Virginia

³ See Feb. 2, 2001, Report of Deborah V. Ellenberg, Chief Hearing Examiner, Case Nos. PUE000343 and PUF000021, Doc. Con. Ctr. No. 010210085 at 12-13.

must be considered in the approval of the construction of this new generating unit. Specifically, §§ 56-46.1, -234.3, -265.2, as well as § 56-580 D of the Code of Virginia apply to this Project. While we have considered the principles embodied by these statutes collectively in reaching our decision in this matter, we will discuss the issues raised by each separately.

Pursuant to §§ 56-234.3 and -265.2 of the Code of Virginia, we consider the following criteria in this application: the need for additional power, the reasonableness of the utility's cost estimates, choice of technology, construction plans, and the availability of suitable alternatives to the project.⁴ Further, we have considered the effect of the proposed facility on the environment as required by §§ 56-46.1 and -580 D of the Code of Virginia. Section 56-46.1 A of the Code of Virginia also permits us to consider the effect of the proposed facility on economic development within the Commonwealth and directs us to consider any improvements in service reliability that may result from the construction of a new generating facility.

In this case, there was no substantial controversy about any of these criteria. The need for electric power within the Northern Virginia service area specifically and Virginia Power's service area generally was acknowledged. As explained in Staff

⁴ The evidence presented in this record indicates that the bids received in response to the Company's recent capacity solicitations would not be better than the Project. Exhibit CDW-12 at 17-18. See also Exhibit JLJ-9 at 4.

witness Walker's testimony, Exhibit CDW-12 at 10-11, the continued load growth in Virginia Power's service territory, as well as the necessity for maintaining adequate generating reserves, is expected to require additional generating resources in the future. Without the Project, reserve margins are expected to be 7.31, 11.53, 9.87, and 7.93 percent in 2003, 2004, 2005, and 2006, respectively. The Project will increase reserve margins to 9.69, 14.01, 12.32, and 10.34 percent in 2003, 2004, 2005, and 2006, respectively. As evidenced by these reserves, additional capacity will be required in the near term, with the exception of 2004, and additional resources will be required in 2003, even with the addition of Unit 6 at Possum Point. Exhibit CDW-12 at 10-11.

As witness Walker also testified, a number of competitive power producers have announced plans to add capacity in Virginia Power's control area, but have not received, and in most cases have not sought, Commission approval to construct and operate these projects. Exhibit CDW-12 at 11-12. Many of these projects may face public opposition that, in turn, may increase the uncertainty that the projects will be successful. Further, there is no evidence that any of these new projects will be available to provide power to Virginia Power. While these plants may be built in Virginia, they may not be contractually

obligated to provide their output to Virginia Power to assist that Company in serving its load.

The Staff also noted that a portion of Virginia Power's future loads may be served by competitive retail suppliers with resources located outside of Virginia Power's service area and that the need for the Project could be decreased by such developments. However, as noted by Staff witness Walker, there is a significant amount of uncertainty as to how much load will be served by these competitive suppliers. Exhibit CDW-12 at 12-14.

In short, considering all of these factors, Virginia Power will require additional generation in the near term future even if Unit 6 is built. Some of this generation may be supplied by the construction of new generating units within the Commonwealth or through the purchase of electric supply elsewhere.

In order to consider whether the Company should be permitted to construct its new unit, we also consider the effects of the Project on the environment. This is a factor that must be weighed along with the need for the unit in determining whether to permit the Company to construct this facility. Specifically, § 56-46.1 A of the Code of Virginia requires that we give consideration to the effect that a proposed facility may have on the environment and directs us to establish such conditions as are necessary to minimize adverse

environmental impacts.⁵ Section 56-580 D of the Code of Virginia directs us to give consideration "to the effect of the facility and associated facilities, including transmission lines and equipment, on the environment and establish such conditions as may be desirable or necessary to minimize adverse environmental impact as provided in § 56-46.1."

As a result of the reconfiguration of the Possum Point Generating Station, i.e., the elimination of two generators burning fuel oil, the conversion of two coal-fired generators to natural gas, continued operation of Unit 5, and the construction of Unit 6, a new unit that will operate on natural gas, Virginia Power will increase its capacity by 32% and will significantly decrease its average emissions for NO_x and SO₂ from this generating station. This is particularly important for this station because it is in a serious ozone nonattainment area. Further, construction of Unit 6 and the reconfiguration of the remaining units at Possum Point will permit the Company to

⁵ Section 56-46.1 also permits us to consider the effect of the facility on economic development within the Commonwealth and directs us to consider any improvements in service reliability that may result from the construction of the subject facility. The testimony in this record indicates that the capacity added by the new unit in Northern Virginia could be interpreted as an economic benefit, in the sense that adding capacity as load grows, decreases supply uncertainty and increases reliability in the Northern Virginia area. Exhibit JS-14 at 7.

Further, the addition of Unit 6 at Possum Point could potentially delay the addition of new transformer banks in Loudoun and Prince William Counties, thus providing additional reliability in the Company's Northern Virginia service area. Exhibit CDW-12 at 14.

reduce emissions in absolute terms while increasing the Company's capacity and generation in a cost effective manner. Exhibit CDW-12 at 22. Exhibit EPH-4 at 3-4.

In its application, Virginia Power has represented that the new unit will be available to serve its growing load, will provide environmental benefits, and will enhance its system reliability. To meet these objectives, Virginia Power must, as a matter of course, maintain and retain control of the new facility at Possum Point. Therefore, the conditions recommended by the Chief Hearing Examiner that require Virginia Power to obtain and maintain control over this facility are appropriate. Subject to the conditions set out in the February 2, 2001, Chief Hearing Examiner's Report, the cost estimates, choice of technology, and manner of construction will meet the Company's growing demand in a timeframe more suitable than any other alternative.⁶

With the addition of the conditions set out in the DEQ coordinated review (Attachment CDW-3 to Exhibit CDW-12), the Project is unlikely to have significant effects on

⁶ While we conclude that the construction of a new unit is needed at Possum Point, we make no determination regarding the transfer of this unit, as that issue will be considered in Virginia Power's Functional Separation Plan Application, docketed as Case No. PUE000584 or in some other docket. In addition, we reach no conclusions as to Virginia Power's proposal to construct a natural gas pipeline lateral, inasmuch as the need for and location of this pipeline was not developed in this case, but is the subject of another Virginia Power application, docketed as Case No. PUE000741.

transportation, forest resources, health issues, and geological features. The Company has agreed to comply with the recommendations found in the DEQ coordinated review. See Exhibit 2. This is a major project, and could have significant impacts on the environment if proper precautions are not undertaken. Accordingly, we will direct our Division of Energy Regulation Staff ("the Division") to monitor Virginia Power's compliance with the recommendations set out in the Chief Hearing Examiner's Report and the coordinated review, and require the Company to provide quarterly reports on its compliance and on its plans to comply with the coordinated review to Staff in advance of its compliance actions. Virginia Power should use all reasonable efforts to comply with the letter and spirit of the coordinated review.

A number of the recommendations set out in the coordinated review permit Virginia Power to take various actions "where practical". The Company should advise Staff in advance when it is not practical for the Company to take an action recommended by the coordinated review and explain why that action is not practical. The Division should review the reports submitted by the Company and consult with the appropriate state agency concerning Virginia Power's plans to comply with the requirements found in the coordinated review (Attachment CDW-3 to Exhibit CDW-12).

Finally, for purposes of this case, we will not find the lessor under the synthetic lease financing for the Project (a Grantor Trust formed to construct and own the new facility and lease it to the sublessor) and the sublessor DEI-Sub, to be public utilities subject to our jurisdiction under the limited circumstances of this case. This finding should be deemed to have no precedential effect in any subsequent, separately docketed proceedings.

Accordingly, IT IS ORDERED THAT:

(1) The findings and recommendations set out on pages 12 and 13 of the Chief Hearing Examiner's February 2, 2001, Report are hereby adopted.

(2) Pursuant to §§ 56-46.1, -234.3, -265.2, and -580 D of the Code of Virginia, Virginia Electric and Power Company is authorized to construct, acquire, and operate the generating units at the Possum Point Power Station, as more specifically described in its June 16 and July 5 applications, i.e., to remove two existing oil-fired units (Units 1 and 2) from service, convert two existing coal-fired units (Units 3 and 4) to natural gas, and construct a new 540 MW combined cycle generating unit at the Possum Point Generating Station in Prince William County, Virginia.

(3) Pursuant to § 56-265.2 of the Code of Virginia, subject to the conditions imposed herein, and upon filing

appropriate maps with the Division of Energy Regulation, Virginia Power shall be granted Certificate of Public Convenience and Necessity No. ET-161 to construct and operate the new 540 megawatt combined cycle facility operating on natural gas or distillate oil identified in Ordering Paragraph (2), as more fully described in the Company's application of June 16, 2000. The Certificate of Public Convenience and Necessity issued herein shall expire if Virginia Power does not obtain or maintain control of this new facility, except as may be determined in Virginia Power's Functional Separation Plan, docketed as Case No. PUE000584 or some other docket. If said Certificate of Public Convenience and Necessity expires, further authority regarding the disposition of the new facility shall be requested from the Commission.

(4) The lessor under the synthetic lease financing for the Project and the sublessor as described more fully herein are not public utilities subject to Commission jurisdiction, based on and limited to the facts of this case.

(5) The financing for the Project, as modified by our Order of November 17, 2000, entered in Case No. PUF000021, and Exhibit 1 attached to Exhibit LTO-13, is hereby approved.

(6) Virginia Electric and Power Company shall comply with all conditions identified as Findings 1 (a)-(f) of the Chief Hearing Examiner's February 2, 2001, Report, as well as the DEQ

coordinated review, so as to minimize any adverse impact in the environment caused by the construction authorized herein. In this regard, Virginia Power shall provide quarterly reports to the Division of Energy Regulation regarding the Company's compliance and plans for compliance with the DEQ coordinated review in advance of actions taken to comply with that review. Where Virginia Power has determined that an action under the coordinated review is not practical, it shall so advise the Division and shall explain in advance why such action is not practical and shall report any actions it has taken to comply with the coordinated review. The Division shall review the reports submitted by the Company and shall consult with the appropriate state agency concerning Virginia Power's plans for compliance.

(7) Consistent with Finding 1 (e) of the February 21, 2001, Hearing Examiner's Report, Virginia Power shall comply with the requirements of the Chesapeake Bay Preservation Act, Chapter 21 (§ 10.1-2100 et seq.) of Title 10.1 of the Code of Virginia, as a further condition of the approval granted herein.

(8) The approvals granted herein are for the specific facilities authorized by this Order, as more particularly described in Virginia Electric and Power Company's applications of June 16, 2000, and July 5, 2000. The Company shall forthwith advise the Commission of any proposed changes to the facilities

or construction practices that differ from those which have been proposed and approved herein.

(9) There being nothing further to be done in this matter, Case Nos. PUE000343 and PUF000021 shall be removed from the Commission's docket of active proceedings, and the papers filed therein made a part of the Commission's file for ended causes.